Supreme Court No. 84855-6

SUPREME COURT OF THE STATE OF WASHINGTON

CERTIFICATION FROM THE UNITED STATES DISTRICT COURT,
EASTERN DISTRICT OF WASHINGTON

IN

CHAD M. CARLSEN and SHASTA CARLSEN;
husband and wife, individually and on behalf of
a Class of similarly situated Washington families; and
CARL POPHAM and MARY POPHAM,
husband and wife, individually and on behalf of
a Class of similarly situated Washington families,

Plaintiffs,

vs.

GLOBAL CLIENT SOLUTIONS, LLC, an Oklahoma limited
liability company; ROCKY MOUNTAIN BANK & TRUST,
a Colorado financial institution; et al.,

Defendants.

OPENING BRIEF

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I. INTRODUCTION

As trying economic times force many families into pressing unsecured credit card debt, a for-profit "debt settlement" industry has arisen, promising consumers a quick and easy resolution of such debt for pennies on the dollar. *See* FTC Telemarketing Sales Rule, 75 Fed. Reg. 48,458 (Aug. 10, 2010) (to be codified at 16 C.F.R. pt. 310).

Unfair and deceptive business practices endemic to this industry, including predatory fee practices, have recently revitalized private and public enforcement of state debt adjusting statutes that have long protected vulnerable consumers from for-profit businesses that purport to help consumers in resolving their debt. 75 Fed. Reg. 48,458, 48463-64 (Aug. 10, 2010) (to be codified at 16 C.F.R. pt. 310) (citing chapter 18.28 RCW as a state statute governing activities of debt settlement companies. *See* 75 Fed. Reg. 48,458, 48464, Fn. 90, 91.).

In the context of class litigation to protect Washington consumers from unfair business activities in the debt settlement industry, the Federal District Court for the Eastern District of Washington has certified unresolved questions of local law pertinent to Washington's Debt Adjusting statute. The District Court's Order Re Certification presents a propitious opportunity to interpret, for the first time, pivotal provisions of the Washington Debt Adjusting Statute, chapter 18.28 RCW, and to

reaffirm Washington's recognition of the common law legal theory of aiding and abetting.

II. STATEMENT OF FACTS

A. Procedural Background.

Plaintiffs Chad M. and Shasta Carlsen (hereinafter "Carlsen") and Carl and Mary Popham (hereinafter "Popham") are Washington consumers who engaged in debt settlement programs involving debt settlement "special purpose accounts." These accounts were established and managed by Global Client Solutions, LLC ("GCS") and "sponsored" by debt settlement companies with whom GCS collaborated. On August 7, 2009, Carlsen and Popham filed a Class Action Complaint in Federal Court for the Eastern District of Washington against GCS and Rocky Mountain Bank & Trust ("RMBT") on behalf of a class of Washington consumers for whom GCS established and managed such "special purpose accounts." **Ct. Rec. 01** *(Complaint)*. Carlsen and Popham also filed related class actions against their respective debt settlement companies with whom GCS collaborated (*Carlsen v. Freedom Debt Relief*, E.D. Wash. No. CV-09-55-LRS; and *Popham v. Silver Bay Financial, Inc.*, Spokane County Superior Court No. 09-2-03585-1).

Plaintiffs' Class Action Complaint against GCS and RMBT, as amended, advances a Consumer Protection Act claim pursuant to chapter

19.86 RCW alleging violation of Washington's Debt Adjusting statute, chapter 18.28 RCW. **Ct. Rec. 83** *(Amended Complaint)*. In that regard, RCW 18.28.185 provides that violation of the Debt Adjusting statute constitutes an unfair and a deceptive act or practice for purposes of chapter 19.86 RCW. Plaintiffs' Class complaint also states a common law claim of liability for having substantially assisted another in the commission of a tort, i.e., a claim for "aiding and abetting," as it is commonly denominated, as well as a claim for breach of fiduciary duty. **Ct. Rec. 83** *(Amended Complaint at pp. 19-22)*.

Defendants responded to the Class Complaint by filing a Motion for Dismissal pursuant to Rule 12(b)(6), Federal Rules of Civil Procedure, claiming Washington's Debt Adjusting statute is inapplicable to their business activities and challenging the existence of a claim for aiding and abetting under Washington law. **Ct. Rec. 18, 28** *(Motions for Dismissal)*. Defendants contemporaneously brought a motion to compel arbitration in Colorado. *See* **Ct. Rec. 40** *(Order Denying Motions)*.

In an "Order Denying Motions to Compel Arbitration, *Inter Alia*" the Federal District Court denied Defendants' Motion to Compel Arbitration and stayed Defendants' Motion for Dismissal in anticipation of certification of questions to this Court. **Ct. Rec. 40** *(Order Denying Motions, pp. 8-9)*.

In order to identify and formulate questions suitable for certification, the District Court directed the parties to conduct limited discovery regarding "the precise nature of GCS and RMBT, and what they do in conjunction with each other, and in conjunction with debt settlement companies." **Ct. Rec. 40** *(Order Denying Motions, p. 8)*. The parties conducted such limited discovery and subsequently filed materials to aid the Court in formulating questions appropriate for certification. *Id.*

On July 23, 2010, the Honorable Judge Lonny R. Suko issued an order of Certification to Washington State Supreme Court in this matter and in the related matter, *Carlsen v. Freedom Debt Relief* (E.D. Wash. No. CV-09-55-LRS).

B. Factual Allegations Framing the Questions Posed.

The District Court's formulation of questions is illuminated by a review of facts alleged in the Complaint and developed through court-ordered discovery.

GCS has entered into contracts with roughly 500 individual debt settlement companies, whereby the respective debt settlement companies agreed to employ GCS's "special purpose accounts" as a key feature of the debt settlement program marketed to indebted consumers. *See* **Ct. Rec. 58-3** *(Ex. P Scott Decl. [Depo. Exhibit 3])*; **Ct. Rec. 58-10** *(Ex. W Scott Decl.)*; **Ct. Rec. 57-14** *(Ex. L Scott Decl. – Hendrix Depo. at pp. 9-13, 20-*

21, 26-28); and **Ct. Rec. 58-13** (*Ex. K Scott Decl. – Hampton Depo. pp. 21-22; 39-40)*. GCS, in turn, agreed to establish, manage, and maintain "special purpose accounts" for the debt settlement companies' customers. *Id.* Consequently, hundreds of debt settlement companies promote debt settlement programs to consumers involving creation of debt settlement "special purpose accounts" created and managed by GCS. *See id.*

Debt settlement companies solicit participation in their plans by providing the consumer with a "Debt Reduction Agreement" or similarly captioned contract with the debt settlement company, a standardized "Special Purpose Account Application" as prepared by GCS, and associated forms and authorizations. **Ct. Rec. 83** (*Amended Complaint* at p. 10); and **Ct. Rec. 58-6** *(Ex. S Scott Decl.)*

Execution of these documents engages the consumer in what debt settlement companies variously term a "debt settlement," "debt management," or "debt reduction" program in which GCS automatically transfers monthly debt settlement payments from the consumer's personal bank account, in amounts specified by the debt settlement company, and into the consumer's "special purpose account." The "special purpose account" is ostensibly created to accumulate funds that are then used by the debt settlement company to attempt settlements with creditors pursuant to the debt settlement plan. **Ct. Rec. 83** (*Amended Complaint* at p. 10).

Although beneficial in theory, the debt settlement programs both obligate the consumer to pay significant up-front debt settlement fees and authorize GCS to automatically pay the debt settlement fees from the "special purpose account" managed by GCS. **Ct. Rec. 83** (*Amended Complaint* at p. 11). The size and timing of debt settlement fees are such that fees consume the monthly debt settlement payments deposited into the "special purpose account" for the first several months of the program. Thereafter, continuing periodic fees significantly consume the debtor's monthly debt settlement payments throughout their participation in the program. **Ct. Rec. 83** *(Amended Complaint* at p. 12*)*.

Debt settlement programs are big business. GCS itself manages approximately 600,000 "special purpose accounts" in collaboration with 500 debt settlement companies. Stated plainly, GCS operates as the central cog in the modern-day debt settlement industry. **Ct. Rec. 83** (*Amended Complaint* at p. 9).

Until recent enforcement efforts by the FDIC against RMBT, GCS's "Special Purpose Account Application," as supplied to consumers by debt settlement companies, appeared to be an application to open a

bank account at RMBT.[1] **Ct. Rec. 83** *(Amended Complaint at p. 10).* In reality, GCS's "Special Purpose Account Application" involves retention of GCS as custodian and fiduciary of the consumer to establish, manage, and maintain a sub-account within a single custodial account that GCS maintains at RMBT. **Ct. Rec. 83** (*Amended Complaint* at p. 10). *See also* **Ct. Rec. 57-12** *(Ex. J Scott Decl. – McClure Depo. pp. 11-17, 23-24);* **Ct. Rec. 57-13** *(Ex. K Scott Decl. – Hampton Depo. pp. 16-17, 28, 29).* GCS aggregates all debt settlement payments of all consumers and deposits them into GCS's single custodial account at RMBT.

GCS maintains a sub-account for individual consumers (the consumer's "special purpose account") within GCS's custodial account, so as to individually account for the proceeds of each consumer. RMBT does

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[1] Similarly, GCS's Account Agreement and Disclosure Statement represented itself as an agreement with RMBT. *See* **Ct. Rec. 58-4** (*Ex. Q Scott Decl.*); **Ct. Rec. 58-6** *(Ex. S Scott Decl.)*; **Ct. Rec. 58-8** (*Ex. U Scott Decl.)*; **Ct. Rec. 58-9** (*Ex. V Scott Decl.)*; **Ct. Rec. 57-13** (*Ex. K Scott Decl. – Hampton Depo. pp. 55, 82-87);* **Ct. Rec. 57-14** (*Ex. L Scott Decl. – Hendrix Depo. pp. 17-19);* **Ct. Rec. 58-13** *(Ex. Z Scott Decl. – Cease and Desist Order).* Following an FDIC Order to Cease and Desist directed at RMBT, GCS's Special Purpose Account Application and Account Agreement and Disclosure Statement either correctly represent themselves as agreements with GCS or, alternatively, fail to disclose the identity of the contracting party. *See* **Ct. Rec. 58-6** *(Ex. S Scott Decl.)*; **Ct. Rec. 58-7** (*Ex. T Scott Decl.)*; **Ct. Rec. 58-9** (*Ex. V Scott Decl.)*; **Ct. Rec. 57-13** *(Ex. K Scott Decl. – Hampton Depo. pp. 55, 82-87)*; **Ct. Rec. 57-14** *(Ex. L Scott Decl. – Hendrix Depo. pp. 17-19)*; and **Ct. Rec. 58-13** *(Ex. Z Scott Decl. – Cease and Desist Order).*

not control the method, manner, or means by which GCS establishes, manages, or maintains its "special purpose" sub-accounts. RMBT does not compensate GCS for its activities. *See* **Ct. Rec. 57-12** *(Ex. J Scott Decl. – McClure Depo. pp. 17-18, 24-25)*; **Ct. Rec. 57-13** *(Ex. K Scott Decl. – Hampton Depo. pp. 37-38). See also* **Ct. Rec. 57-15** *(Ex. M Scott Decl. – Merrick Depo. pp. 24-25)*; **Ct. Rec. 57-14** *(Ex. L Scott Decl. – Hendrix Depo. p. 44).*

RMBT does, however, benefit from its bank/customer relationship with GCS. It holds substantial funds interest-free in GCS's custodial account. GCS's custodial account at RMBT constituted roughly fifty percent of all deposits at RMBT at the time of the FDIC's Order to Cease and Desist directed at RMBT. *See* **Ct. Rec. 58-13** *(Ex. Z Scott Decl. – Cease and Desist Order)*; **Ct. Rec. 57-12** *(Ex. J Scott Decl. – McClure Depo. p. 17)*; **Ct. Rec. 57-15** *(Ex. M Scott Decl. – Merrick Depo. p. 39)*; **Ct. Rec. 57-13** *(Ex. K Scott Decl. – Hampton Depo. p. 57).*[2]

In the context of these underlying factual allegations, the district court has certified the following questions of local law.

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[2] The "Schedule of Fees and Charges" shown on GCS's "Special Purpose Account Application," likewise, are not banking fees or charges of RMBT, as they appear. The fees and charges are those of GCS. GCS makes its profit by charging these fees and charges. *See* **Ct. Rec. 57-13** *(Ex. K Scott Decl. – Hampton Depo. pp. 41-43)*; **Ct. Rec. 57-14** *(Ex. L Scott Decl. – Hendrix Depo. p. 44).*

III. QUESTIONS PRESENTED AND SUMMARY OF ANSWERS

Question 1: *Is a for-profit business engaged in "debt adjusting" as defined in RCW 18.28.010(1) when, in collaboration with debt settlement companies, it: a) establishes and maintains a custodial bank account in its name; b) solicits debtors' establishment of a sub-account to receive and hold periodic payments to be used to pay debt settlement fees and pay settlements with creditors as negotiated by a debt settlement company; and c) as custodian for the debtor, receives and holds the debtor's periodic payments in a sub-account, paying from that account debt settlement fees and negotiated settlements with creditors?*

ANSWER: **Yes. The business of receiving funds for the purpose of distributing those funds among creditors to settle the indebtedness of a debtor constitutes "debt adjusting" within the meaning of RCW 18.28.010(1).**

Question 2: *Does the exclusion found at RCW 18.28.010(2)(b) apply to a for-profit business described in Question No. 1?*

ANSWER: **No. The "banking" exclusion found at RCW 18.28.010(2)(b) excludes financial institutions licensed and regulated under applicable bodies of state or federal law; the "banking" exclusion does not extend to non-financial institutions.**

Question 3: *Do the fee limitations set forth in RCW 18.28.080 apply to for-profit debt settlement companies engaged in soliciting the participation of debtors in a debt management program involving: a) monthly set aside and accumulation of a debtor's funds in a custodial account for the purposes of facilitating negotiated settlement of specified credit card debts; and b) negotiations by the debt settlement company, on behalf of the debtor, to secure compromise settlement of the debtor's credit card debt, to be paid from the custodial account?*

ANSWER: **Yes. A business is engaged in "settling," "adjusting," "liquidating," or "managing" the indebtedness of a debtor, within the meaning of RCW 18.28.010, when it undertakes the task of negotiating compromise settlements of debts on behalf of an indebted consumer. Such a company is engaged in "debt adjusting" without regard for whether it directly receives funds from the debtor for purposes of paying the compromise settlement. A company that engages in such activities for compensation is a "debt adjuster" within the meaning of RCW 18.28.010(2). It is, therefore, subject to the fee limitations set forth in RCW 18.28.080.**

Question 4: *Does the Debt Adjusting statute provide for an implied civil action against an alleged "aider or abettor" where aiding or abetting a violation of the Debt Adjusting statute is expressly made a crime pursuant to RCW 18.28.190?*

ANSWER: **Washington law imposes common law civil liability on one who gives substantial assistance to another in the commission of a tort (commonly denominated aiding and abetting.) The Debt Adjusting Act's criminalization of aiding and abetting is immaterial to the existence of such civil liability.**

IV. ARGUMENTS

A. A Company That Receives and Accumulates a Debtor's Funds for the Purpose of Promoting Settlements with Various Creditors and Who Distributes Such Funds Among Creditors in Accordance With Such Settlements, is Engaged in "Debt Adjusting" Within the Meaning of RCW 18.28.010(1).

Washington's Debt Adjusting statute was adopted to protect consumers from unfair business practices endemic to the for-profit debt adjusting industry. *See* Performance Audit of Debt Adjusting, Licensing and Regulatory Activities, Report No. 77-13, Jan. 20, 1978 at p. 11 (on file with Wash. State Archives, H.B. 86 (Wash. 1979)). As a remedial statute, Washington's Debt Adjusting statute is broadly construed. *See, e.g., State v. Pike,* 118 Wn.2d 585, 591, 826 P.2d 152 (1992) ("As a remedial statute, the [Automotive Repair Act] is to be liberally construed to further this legislative purpose."); *Silverstreak, Inc. v. Dep't of Labor & Indus.*, 159 Wn.2d 868, 882, 154 P.3d 891 (2007) ("[T]he prevailing wage act is remedial legislation designed to protect the employees of government contractors in this state from substandard earnings and to preserve local wage standards. As such, the act and regulations promulgated thereunder are to be liberally construed in favor of the

beneficiary of the act, the worker."); *see also* RCW 18.28.185 (violation of the Washington Debt Adjusting statute "constitutes an unfair or deceptive act or practice" under the Washington Consumer Protection Act).

The first rule in statutory interpretation is that "the court should assume that the legislature means exactly what it says. Plain words do not require construction." *Davis v. Dep't of Licensing*, 137 Wn.2d 957, 963-64, 977 P.2d 554 (1999) (quoting *State v. McCraw*, 127 Wn.2d 281, 288, 898 P.2d 838 (1995)). To this end, four factors guide the Court in determining the plain meaning of a term: "[T]he ordinary meaning of the language at issue, the context of the statute in which that provision is found, related provisions, and the statutory scheme as a whole." *Christensen v. Ellsworth*, 162 Wn.2d 365, 373, 173 P.3d 228 (2007).

State statutes governing for-profit debt settlement businesses invariably designate a term to define the business activities subject to the statute. Irrespective of the term chosen, the statutory definitions treat the question as to whether *receipt* of the debtor's funds is necessary or is sufficient for the statute to apply. State debt adjusting statutes align themselves into two camps: (1) those that make actual or constructive

receipt of the debtor's funds a requirement for the statute's application;[3] and (2) those that make receipt and distribution of the debtor's funds a sufficient but non-essential condition for application of the statute.[4] Washington's Debt Adjusting statute unambiguously aligns itself with the second camp. *See generally* RCW 18.28.010(1).

Washington's Debt Adjusting statute identifies alternative activities constituting "debt adjusting," including receipt of funds for the purpose of distributing funds among creditors. Specifically, RCW 18.28.010(1) reads: "'Debt Adjusting' means the managing, counseling, settling, adjusting, prorating, or liquidating of the indebtedness of a debtor,

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[3] *See,* ARIZ. REV. STAT. § 6-701(4); ARK. CODE ANN. § 5-63-301(2); CAL. FIN. CODE § 12002.1; CONN. GEN. STAT. § 36A-655; DEL. CODE ANN. Tit. 11, § 910; ILL. COMP. STAT. 205/665-2; IND. CODE § 28-1-29-1(2); MD. CODE ANN., Fin. Inst., § 12-901(g); MICH. COMP. LAWS ANN. § 451.412(d); MINN. STAT. ANN. § 332A.02 (Subd. 9); MO. REV. STAT. § 425.010(1); NEB. REV. STAT. § 69-1201(1); NEV. REV. STAT. § 676.040; N.M. STAT. ANN. § 56-2-1(B); 63 PA. STAT. ANN. § 2402.

[4] *See,* GA. CODE ANN. § 18-5-1(1); HAW. REV. STAT. § 446-1(2); IOWA CODE § 533A.1(2); KAN. STAT. ANN. § 50-1117(d); KY. REV. STAT. ANN. § 380.010(2); LA. REV. STAT. ANN. § 14:331(B)(2); ME. REV. STAT. ANN. Tit. 32, § 6172(2); MASS. GEN. LAWS Ch. 180, §4A; MISS. CODE ANN. § 81-22-3(b); MONT. CODE ANN. § 30-14-2101(1)(a); N.H. REV. STAT. ANN. § 399-D:2(IV); N.J. STAT. ANN. § 17:16G-1(c)(1) and N.J. Admin. Code Tit. 3, § 3:25-1.1; N.C. GEN. STAT. § 14-423(2); N.D. CENT. CODE § 13-06-01(1); OHIO REV. CODE ANN. § 4710.01(B); OR. REV. STAT. § 697.602(2); S.D. CODIFIED LAWS § 37-34-1; TENN. CODE ANN. § 47-18-104(a)(39)(C); TEX. FIN. CODE ANN. § 394.202(6); VT. STAT. ANN. Tit. 8, § 4861(2); RCW 18.28.010(1); WYO. STAT. ANN. § 33-14-101(a)(ii).

or receiving funds for the purpose of distributing said funds among creditors in payment or partial payment of obligations of a debtor." RCW 18.28.010(1) (emphasis added).

"When a statutory term is undefined, the words of a statute are given their ordinary meaning, and the court may look to a dictionary for such meaning." *State v. Gonzalez*, 168 Wn.2d 256, 263, 226 P.3d 131 (2010). "The dictionary describes 'or' as a 'function word' indicating 'an *alternative* between different or unlike things.'" *Lake v. Woodcreek Homeowners Ass'n*, 168 Wn.2d 694, 706, 229 P.3d 791 (2010) (emphasis in original) (quoting WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 1585 (2002)); *see also People v. Miklos*, 914 N.E.2d 506, 509 (Ill. App. Ct. 2009) ("The word 'or' is disjunctive."); *Elementary Sch. Dist. 159 v. Schiller*, 849 N.E.2d 349, 359 (Ill. 2006) ("In other words, 'or' means 'or.'").[5]

The activities identified in RCW 18.28.010(1) as constituting "debt adjusting" are separated by commas and the disjunctive term "or," thus

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[5] *Cf. HJS Dev. v. Pierce County*, 148 Wn.2d 451, 474 n.95, 61 P.3d 1141 (2003) ("Statutory phrases separated by the word 'and' generally should be construed in the conjunctive.")

identifying various activities constituting debt adjusting.[6] The stand-alone clause "or receiving funds for the purpose of distributing said funds among creditors," thus, designates an activity constituting "debt adjusting" apart from such activities as "the managing, counseling, settling, adjusting, prorating, or liquidating of the indebtedness of a debtor," (each of which also constitutes "debt adjusting").

"When . . . the statutory terms are plain and unambiguous, we assume the legislature meant exactly what it said and decline to construe the statute otherwise." *See Burton v. Lehman*, 153 Wn.2d 416, 424, 103 P.3d 1230 (2005). That is the case here.[7]

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[6] *Compare with* ILL. COMP. STAT. 205/665-2 ("'Debt management service' means the planning and management of the financial affairs of a debtor for a fee *and the receiving of money from the debtor* for the purpose of distributing it . . .") (emphasis added).

[7] The legislature aptly distinguished between the terms "and" and "or" as conjunctive and disjunctive terms elsewhere within RCW 18.28.010(1) and in other sections of chapter 18.28 RCW. *See, e.g.*, RCW 18.28.090(1) (making void any contract and requiring the return of the debtor's payments when a debt adjuster "contracts for, receives *or* makes any charge" in excess of the maximums allowed by Washington law) (Emphasis added); RCW 18.28.130(1) (debt adjusters shall not "Prepare, advise, *or* sign a release of attachment *or* garnishment, stipulation, affidavit for exemption, compromise agreement *or* other legal *or* court document.") (emphasis added); RCW 18.28.010(2)(b) (setting forth a list of entities that may be exempt from the statute, including entities "doing business under and as permitted by any law of this state *or* of the United States relating to banks, ... title insurance companies, *or* insurance companies...") (emphasis added).

The meaning of the term "receiving funds for the purpose of distributing said funds among creditors" is informed by both its context and association with other activities identified as constituting "debt adjusting." The term "distribute" means to "divide among several or many: deal out: apportion esp. to members of a group or over a period of time." WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY, unabridged 660 (2002), s.v. "Distribute." A company that collaborates with debt settlement companies by serving as custodian and manager of debt settlement funds, accumulated over time, for the express purpose of achieving compromise settlements with multiple creditors, and who ultimately allocates those funds among those creditors in accordance with settlements achieved, is clearly engaged in "distributing funds among creditors" within the meaning and contemplation of Washington's Debt Adjusting statute. The first question posed by the district court, therefore, sets forth conditions constituting "debt adjusting" within the meaning of RCW 18.28.010(1).

B. The "Banking" Exclusion Found at RCW 18.28.010(2)(b) Excludes Financial Institutions Licensed and Regulated Under Identifiable Bodies of State or Federal Law; the "Banking" Exemption Does Not Extend to a Business That is Not a Financial Institution.

Exemptions from remedial legislation are narrowly construed in a manner that is consistent with the terms and spirit of that legislation. *Silverstreak, Inc.*, 159 Wn.2d at 882 (citing *Drinkwitz v. Alliant Techsystems, Inc.*, 140 Wn.2d 291, 301, 996 P.2d 582 (2000); *Knecht v. Redwood City*, 683 F. Supp. 1307, 1310 (N.D. Cal. 1987)); *see also Singleton v. Naegeli Reporting Corp.*, 142 Wn. App. 598, 607, 175 P.3d 594 (2008) ("[C]ourts must narrowly construe the scope of the exemption provisions of the CPA."). In this regard, RCW 18.28.010(2)(b) excludes from the term "debt adjuster":

> Any person, partnership, association, or corporation doing business under and as permitted by any law of this state or of the United States relating to banks, consumer finance businesses, consumer loan companies, trust companies, mutual savings banks, savings and loan associations, building and loan associations, credit unions, crop credit associations, development credit corporations, industrial development corporations, title insurance companies, or insurance companies.

The clause "doing business under and as permitted by any law of this state or of the United States" denotes enterprises whose existence and activities are regulated by an identifiable body of federal or state statutory law. Significantly, all of the business forms identified within the "related

to" clause of RCW 18.28.010(2)(b) are derived from the titles of Washington statutes as they existed through the date of the statutes' last revision in 1999[8] and/or are institutional forms transferred to the Department of Financial Institutions for regulation.[9]

In interpreting a virtually identical exemption found in Washington's Small Loan Act, Laws of 1941, ch. 208 p. 609, the court in *Kelleher v. Minshull,* 11 Wn.2d 380, 390, 119 P.2d 302 (1941) explained the legislature's intent: "In making the classification that it did, the legislature undoubtedly concluded that the persons exempted from the

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[8] *See, e.g.,* Banks and Trust Companies, Title 30 RCW; Consumer Loan Act, Chapter 31.04 RCW; Credit Unions, Chapter 31.12 RCW; Mutual Savings Banks, Title 32 RCW; Insurance, Title 48 RCW.

[9] The **Department of Financial Institutions (DFI)** was created in 1993. There are four regulatory Divisions within the Department, including:

- Division of Banks;
- Division of Credit Unions;
- Division of Securities; and
- Division of Consumer Services.

The latter Division regulates mortgage brokers, consumer loan companies, escrow agents, check cashers and sellers, and payday lenders. The Division of Consumer Services enforces statutes and regulations primarily focused on disclosure compliance, lending restrictions, trust accounting and other consumer protections. While the Divisions of Banks and Credit Unions are the primary regulators for the banking and credit union industries, their mission does not include direct responsibility for consumer compliance and protection issues. These areas fall within the jurisdiction of the federal banking and credit union regulators. *See* Washington State Department of Financial Institutions, http://www.dfi.wa.gov/about.htm (last visited August 30, 2010).

operation of the act were sufficiently regulated and controlled by the terms of specific statutes previously enacted to regulate such persons and the businesses in which they are engaged." *Id.* The "banking" exclusion contained in RCW 18.28.010(2)(b), therefore, exempts financial institutions performing banking activities pursuant to state or federal banking law.

Courts, further, must remain careful to avoid "unlikely, absurd or strained" results when interpreting statutes. *Burton v. Lehman*, 153 Wn.2d at 423 (quoting *State v. Stannard*, 109 Wn.2d 29, 36, 742 P.2d 1244 (1987)). An expansive reading of the exemption found at RCW 18.28.010(2)(b), in this regard, would render the Debt Adjusting statute's consumer protections illusory. RCW 18.28.150 requires that every debt adjuster hold payments received from a debtor in trust and take a number of other particularized steps in the management of such funds. These are functions invariably performed in conjunction with some bank. If performing these functions were to bring a business within the banking exemption, the exemption would eviscerate the consumer protections afforded by chapter 18.28 RCW.

A private for-profit non-financial institution engaged in managing debt settlement funds in collaboration with debt settlement companies is not "doing business under and as permitted by the laws of this state or of

the United States relating to banks." It is not, therefore, exempt from the consumer protections afforded by chapter 18.28 RCW.

C. The Fee Limitations Found at RCW 18.28.080 are Applicable to a For-Profit Company Engaged in Settling Consumer Debt.

A principal purpose of state debt adjusting statutes is protection of consumers from predatory fee practices. Washington's provision is codified at RCW 18.28.080:

> By contract a debt adjuster[10] may charge a reasonable fee for debt adjusting services. The total fee for debt adjusting services may not exceed fifteen percent of the total debt listed by the debtor on the contract. The fee retained by the debt adjuster from any one payment made by or on behalf of the debtor may not exceed fifteen percent of the payment. The debt adjuster may make an initial charge of up to twenty-five dollars which shall be considered part of the total fee. If an initial charge is made, no additional fee may be retained which will bring the total fee retained to date to more than fifteen percent of the total payments made to date.

Washington's statute, therefore, both caps the total fees chargeable and prohibits the "front-loading" of fees, and these limitations apply to for-profit companies engaged in settling consumer debt.

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[10] The term "debt adjuster," is statutorily defined by reference to the activities denominated "debt adjusting" under the statute: "'Debt adjuster[']. . . is any person engaging in or holding himself or herself out as engaging in the business of debt adjusting for compensation . . ." RCW 18.28.010(2).

RCW 18.28.010(1) expressly includes "settling . . . of the indebtedness of a debtor" as an activity constituting "debt adjusting." A company that, for compensation, engages in the business of settling the indebtedness of debtors, therefore, is plainly engaged in "debt adjusting" as it is statutorily defined.

Washington's inclusion of settlement activities within the scope of "debt adjusting" is neither inadvertent nor anomalous. The debt adjusting statutes in Wyoming, Ohio, Georgia, and North Carolina, all of which preceded Washington's adoption of debt adjusting legislation, similarly defined the term "debt adjusting" expansively so as to include the settling of a debtor's debt.[11]

The fee limitations of RCW 18.28.080 apply to a "debt adjuster," a term meaning "any person engaging in or holding himself or herself out as engaging in the business of debt adjusting for compensation." RCW 18.28.010(2) (emphasis added). A for-profit business engaged in settling

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[11] North Carolina's statute, for example, included: "settling, compounding, or in anyway altering the terms of payment of any debt of a debtor[.]" N.C. GEN. STAT. § 14-423(2) (1963); *see also* WYO. STAT. ANN. § 33-14-101(a)(ii) (1957) ("Effecting the adjustment, compromise, or discharge of any account, note, or other indebtedness"); OHIO REV. CODE ANN. § 4710.01(B) (1958) ("[T]o effect the adjustment, compromise, or discharge of any account, note or other indebtedness of the debtor."); GA. CODE ANN. § 18-5-1(1) (1956) ("[to] effect the adjustment, compromise, or discharge of any account, note, or other indebtedness of the debtor.").

the indebtedness of a debtor is, therefore, clearly subject to the fee limitations found at RCW 18.28.080.

The receipt of funds, it should be noted, is not a necessary condition for settlement activity to fall within the statutory definition of "debt adjusting." Whether a for-profit business itself receives and holds the funds used to accomplish settlement or collaborates with another company to receive, accumulate, and ultimately distribute settlement funds is wholly immaterial to the applicability of the statutory fee limitations.[12]

In keeping with the statutory definition of "debt adjusting," RCW 18.28.080 purposefully does not confine its fees limitation to a percentage of payments received by the debt adjuster. The fee provision as originally

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[12] Washington's Debt Adjuster statute also stands against the contextual backdrop of other comparable state statutes with respect to the receiving and distribution of debtors' funds. The Debt Adjusting statutes of Georgia, Wyoming, and Ohio provide that one who is engaged in effecting the compromise of a debtor's debt was engaged in debt adjusting regardless as to whether funds were received or distributed. GA. CODE ANN. § 18-5-1(1) (1956); WYO. STAT. ANN. § 33-14-101(a)(ii) (1957); OHIO REV. CODE ANN. § 4710.01(B) (1958). At the time Washington's statute was enacted, North Carolina alone expressly made the receipt of the consumer's funds a necessary condition for the activity to constitute "debt adjusting." *See* N.C. GEN. STAT. § 14-423(2) (1963); *cf. Ball-Foster Glass Container Co. v. Giovanelli*, 163 Wn.2d 133, 140-41, 177 P.3d 692 (2008) ("The language of ... [a particular] statute shows the intent of the Washington Legislature to adopt a broader and more comprehensive statute than other states."). This point of contrast between Washington and North Carolina also reinforces the plain meaning of the Washington statute. *See also Danny v. Laidlaw Transit Servs., Inc.*, 165 Wn.2d 200, 193 P.3d 128 (2008).

enacted in 1967 provided that a debt adjuster could not take from any one payment "more than fifteen percent of the amount *received by it* . . . ." Laws of 1967, ch. 201, § 8. (Emphasis added). However, RCW 18.28.080(1) was revised in 1979 to provide that this restriction applied to "The fee retained by the debt adjuster from any one payment made by or on behalf of the debtor," without restriction as to the party receiving the payment. RCW 18.28.080(1) (rev. 1979). In revising a statute, the legislature is presumed to have either changed the law or clarified a previous ambiguity. *Bowen v. Statewide City Employees Ret. Sys.*, 72 Wn.2d 397, 402-03, 433 P.2d 150 (1967). This revision is in keeping with the statute's intent of protecting consumers from rapacious debt adjuster fees, whether the debt adjuster receives the consumer's debt settlement payments, or in the instant case, collaborates with another for-profit company to receive and manage the debt settlement funds.

In interpreting statutes, further, courts keep in mind the mischief sought to be met. *See generally Giuricevic v. Tacoma*, 57 Wash. 329, 106 P. 908 (1910). RCW 18.28.080 is aimed at ensuring that already indebted consumers are not further burdened by excessive fees or heavily front-loaded fees. Whether unscrupulous debt settlement companies secure excessive or front-loaded fees from debt settlement payments directly received by them, or received by a third-party custodian provided for

under the applicable debt settlement plan, is immaterial to the harm the statute seeks to address. Reading into the statute a limitation that the fee restrictions apply only to payments directly received by the debt settlement company would allow the mischief the statute seeks to restrain.

D. Washington Recognizes a Common Law Claim for Aiding and Abetting Whose Elements are Articulated in the RESTATEMENT (SECOND) OF TORTS § 876.

Washington, like other jurisdictions, recognizes a common law claim whereby a secondary actor may be derivatively liable for assisting a primary actor, who by virtue of his own actions, causes harm to the plaintiff. The theory of civil aiding and abetting, rooted in common law, is currently encapsulated within Section 876(b) of the Restatement (Second) of Torts:

> For harm resulting to a third person from the tortious conduct of another, one is subject to liability if he:
>
> (a) does a tortious act in concert with the other or pursuant to a common design with him, or
>
> (b) **knows that the other's conduct constitutes a breach of duty and gives substantial assistance or encouragement to the other so to conduct himself,** or
>
> (c) gives substantial assistance to the other in accomplishing a tortious result and his own conduct, separately considered, constitutes a breach of duty to the third person.

RESTATEMENT (SECOND) OF TORTS § 876(b) (1979) (emphasis added).

Under subsection (b), the section pertinent to the present case, a party is subject to liability for harm resulting to a third person from the tortuous conduct of another if he both knows the other's conduct constitutes a breach of duty and gives substantial assistance to the other. *Id.* § (b). *See* 86 C.J.S. *Torts* § 105 (West updated 2009) ("As a general rule, one who counsels, advises, abets, or assists the commission of an actionable wrong by another is responsible to the injured person for the entire loss or damage."); *see also Landy v. Fed. Deposit Ins. Corp.*, 486 F.2d 139, 162-63 (3d Cir. 1973); *Petro-Tech, Inc. v. Western Co. of N. Am.*, 824 F.2d 1349, 1357 (9th Cir. 1987) ("[This] Restatement provision has been applied by a number of state and federal courts in civil litigation.").[13]

Washington quoted Section 876 with approval as early as 1956 in *Thomas v. Casey*, 49 Wn.2d 14, 297 P.2d 614 (1956). Since then, our courts have routinely reaffirmed both the particular Restatement Section

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[13] *See also* Nathan Isaac Combs, *Civil Aiding and Abetting Liability*, 58 VAND. L. REV. 241, 256 (2005) ("In sum, the Restatement provides the following basic requirements for civil aiding and abetting liability: (1) that a tortious act be committed by the primary tortfeasor; (2) that the defendant know that the primary tortfeasor's conduct constitutes a breach of some duty; (3) that the defendant provide substantial assistance or encouragement to the breach of that duty; and (4) that the defendant's assistance or encouragement constitute a proximate cause of the resulting tort or torts.").

itself and the legal principle it embodies—where an entity participates in the wrongful act of a third party by aiding and abetting that wrong, that entity assumes liability for the wrongful act. *See, e.g., La Hue v. Keystone Inv. Co.*, 6 Wn. App. 765, 783, 496 P.2d 343 (1972);[14] *see generally Martin v. Abbott Labs.*, 102 Wn.2d 581, 596, 689 P.2d 368 (1984)

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[14] California has published a useful explanation discussing the distinctions between conspiracy, aiding and abetting, and other forms of derivative liability:

> [The] imposition of derivative liability is not limited to the doctrine of respondeat superior. Liability based on an aiding and abetting or conspiracy theory is also "derivative," i.e., liability is imposed on one person for the direct acts of another. "Conspiracy is not a cause of action, but a legal doctrine that imposes liability on persons who, although not actually committing a tort themselves, share with the immediate tortfeasors a common plan or design in its perpetration. [Citation.] By participation in a civil conspiracy, a coconspirator effectively adopts as his or her own the *torts of other coconspirators* within the ambit of the conspiracy." (*Applied Equip. Corp. v. Litton Saudi Arabia Ltd.*, 7 Cal. 4th 503, 510-511 (1994), italics added). Similarly, aiding and abetting liability may "'be imposed on one who aids and abets the commission of an intentional tort if the person (a) knows the *other's conduct* constitutes a breach of a duty and give substantial assistance or encouragement *to the other* to so act or (b) gives substantial assistance *to the other* in accomplishing a tortious result and the person's own conduct, separately considered, constitutes a breach of duty to the third person.'" (*Fiol v. Doellstedt, supra*, 50 Cal. App. 4th at pp. 1325-26, italics added).

Richard B. LeVine, Inc. v Higashi, 131 Cal. App. 4th 566, 579, 32 Cal. Rptr. 3d 244 (2005).

(discussing various theories of liability) (citing *Abel v. Eli Lilly & Co.*, 418 Mich. 311, 343 N.W2d 164, 176 (1984); *Rody v. Hollis*, 81 Wn.2d 88, 94, 500 P.2d 97 (1972); *Cain v. Dougherty*, 54 Wn.2d 466, 341 P.2d 879 (1959); *Martin v. Sikes*, 38 Wn.2d 274, 278-79, 229 P.2d 546 (1951); *Westview Invs., Ltd. v. U.S. Bank*, 133 Wn. App. 835, 138 P.3d 638 (2006); *Ed Nowogroski Ins., Inc. v. Rucker*, 88 Wn. App. 350, 355, 944 P.2d 1093 (1997).

A review of authority from our sister jurisdictions reinforces Section 876(b) as an apt statement of the common law doctrine of civil aiding and abetting. *See, e.g., El Camino Res., Ltd. v. Huntington Nat'l Bank*, 2009 U.S. Dist. LEXIS 128084 at *46 (W.D. Mich. 2009) ("Although not using the words 'aiding and abetting,' section 876(b) is generally recognized as describing a concept of secondary liability similar to the criminal concept of aiding and abetting a crime."); *Wells Fargo Bank v. Ariz. Laborers, Teamsters & Cement Masons Local No. 395 Pension Trust Fund*, 201 Ariz. 474, 485, 39 P.3d 12, 23 (2002) ("Arizona recognizes aiding and abetting as embodied in Restatement § 876(b), that a person who aids and abets a tortfeasor is himself liable for the resulting harm to a third person."); *see also Aetna Cas. & Sur. Co. v. Leahey Constr. Co.*, 219 F.3d 519, 533-34 (6th Cir. 2000); *Steelvest, Inc. v. Scansteel Serv. Ctr., Inc.*, 807 S.W.2d 476, 485 (Ky. 1991).

A highly instructive case to this effect is *Halberstam v. Welch*, 705 F.2d 472 (D.C. Cir. 1983). There, the Court of Appeals for the District of Columbia emphasized the important distinctions between subsections (a) and (b) of Restatement Section 876:

> Over time, courts applied the principle of vicarious liability for concerted action to less obvious situations, covering tortfeasors whose relationship was more subtle than Prosser's "highwaymen." The two variations significant here are (1) *conspiracy, or concerted action by agreement*, and (2) *aiding-abetting, or concerted action by substantial assistance*. These two bases of liability correspond generally to the first two subsections in the Restatement (Second) of Torts § 876 (1979) . . . .

Halberstam, 705 F.2d at 477 (emphasis in original). The court continued by aptly distinguishing civil conspiracy from aiding and abetting:

> The element of agreement is a key distinguishing factor for a civil conspiracy action. Proof of a tacit, as opposed to explicit, understanding is sufficient to show agreement. But the agreement in a civil conspiracy does not assume the same importance it does in a criminal action. To establish liability, the plaintiff also must prove that an unlawful overt act produced an injury and damages.
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> . . .
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> Aiding-abetting includes the following elements: (1) the party whom the defendant aids must perform a wrongful act that causes an injury; (2) the defendant must be generally aware of his role as part of an overall illegal or tortious activity at the time that he provides the assistance; (3) the defendant must knowingly and substantially assist the principal violation. In the "Comment on Clause (b)," the authors of the *Restatement* summarize these elements and explain why they create liability: "Advice or encouragement to act operates as a moral support to a

> tortfeasor and if the act encouraged is known to be tortious it has the same effect upon the liability of the adviser as participation or physical assistance."
>
> . . .
>
> The prime distinction between civil conspiracies and aiding-abetting is that a conspiracy involves an agreement to participate in a wrongful activity. Aiding-abetting focuses on whether a defendant knowingly gave "substantial assistance" to someone who performed wrongful conduct, not on whether the defendant agreed to join the wrongful conduct.

Id. at 477-78 (internal citations omitted).[15]

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[15] The *Halberstam* court continued:

> Courts and commentators have frequently blurred the distinction between the two theories of concerted liability. Most commonly, courts have relied on evidence of assistance to the main tortfeasor to infer an agreement, and then attached the label "civil conspiracy" to the resultant amalgam. Sometimes, although not always, the inference has been factually justified; many tort defendants have both conspired with and substantially assisted each other. But we find it important to keep the distinctions clearly in mind as we review the facts in this novel case to see if tort liability is warranted on either or both concerted action theories. For the distinctions can make a difference. There is a qualitative difference between proving an *agreement to participate* in a tortious line of conduct, and proving *knowing action* that substantially aids tortious conduct. In some situations, the trier of fact cannot reasonably infer an agreement from substantial assistance or encouragement. A court must then ensure that all the elements of the separate basis of aiding-abetting have been satisfied. For example, *Rael v. Cadena*, 93 N.M. 684, 604 P.2d 822 (1979) . . . involved aid that was unlikely to support a conclusion of agreement. Furthermore, it is difficult to

In addition to the above authority and analysis from the D.C. Circuit, numerous Ninth Circuit opinions acknowledge this theory of liability. For example, *Henry v. Lehman Commer. Paper, Inc. (In re First Alliance Mortg. Co.)*, 471 F.3d 977 (9th Cir. 2006) is both illustrative of Section 867(b)'s theory of aiding and abetting liability and analogous to the present case.

In *Henry*, the bankruptcy trustee advanced a claim on behalf of a class of consumers that Lehman Brothers, Inc. aided and abetted[16] First Alliance Mortgage Company (the subprime mortgage lender that filed for bankruptcy) in fraudulent lending practices. *In re First Alliance Mortg. Co.*, 298 B.R. 652, 667 (C.D. Cal. 2003). The First Alliance loan officers made sales presentations and used methods to convince borrowers to enter into loans that contained "hidden egregious loan origination fees (points),

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> conceive of how a conspiracy could establish vicarious liability where the primary wrong is negligence, but a secondary defendant could substantially aid negligent action. The theory of liability also affects who is liable for what. An aider-abettor is liable for damages caused by the main perpetrator, but that perpetrator, absent a finding of conspiracy, is not liable for the damages caused by the aider-abettor.

Halberstam, 750 F.2d at 478.

[16] California law on aiding and abetting is consistent with Section 876(b) of the Restatement of Torts. *See, e.g., Saunders v. Superior Court*, 27 Cal. App. 4th 832, 33 Cal. Rptr. 2d 438, 446 (Cal. Ct. App. 1994).

other 'junk' fees, and prepaid interest." *Id.* These methods, according to the Court, constituted fraud by First Alliance, of which Lehman both knew and substantially assisted through its satisfaction of First Alliance's financial needs, resulting in Lehman's liability. *Id.*

Similarly, aiding and abetting (also known as "aiding and assisting") is recognized as a basis of recovery in Oregon. Indeed, as early as 1899, the Oregon Supreme Court declared:

> [A]ll who aid, command, advise, or countenance the commission of a tort by another, or who approve of it after it is done, if done for their benefit, are liable in the same manner as they would be if they had done the same tort with their own hands.

Perkins v. McCullough, 36 Ore. 146, 149, 59 P. 182 (1899) (quoting *Judson v. Cook*, 11 Barb. 642 (N.Y. 1852)). Subsequently, the Oregon courts have repeatedly quoted Section 876(b) with approval. *See generally Granewich v. Harding*, 329 Ore. 47, 985 P.2d 788 (Ore. 1999); *Lemons v. Kelly*, 239 Ore. 354, 397 P.2d 784 (Ore. 1964).

Jurisdictions outside of the Ninth Circuit have similarly embraced the concept of civil liability for aiding and abetting another in the commission of a tort. *See generally Estate of Axelrod v. Flannery*, 476 F. Supp. 2d 188, 195 (D. Conn. 2007); *Infosage, Inc. v. Mellon Ventures, L.P.*, 896 A.2d 616 (Pa. Super. Ct. 2006); *Wells Fargo Bank v. Ariz. Laborers, Teamsters and Cement Masons Local No. 395 Pension Trust*

Fund, 201 Ariz. 474, 485, 39 P.3d 12, 23 (2002); *Lindsay v. Lockwood*, 163 Misc. 2d 228, 625 N.Y.S.2d 393 (1994); *Rael v. Cadena*, 93 N.M. 684, 604 P.2d 822 (N.M. Ct. App. 1979). Clearly, this basis for liability is deeply embedded in the common law and Washington's approach comports therewith.

RCW 18.28.190 criminalizes violation of the Debt Adjusting act, including aiding and abetting such violation. This provision, however, is not the birthplace of civil liability for aiding and abetting. Civil liability for aiding and abetting under Washington law is grounded in common law as articulated in the RESTATEMENT (SECOND) OF TORTS § 876(b).

V. CONCLUSION

Plaintiffs, therefore, respectfully request that this Court answer the questions posed by the District Court in the manner set forth in this Brief.

Respectfully Submitted this 30th day of August, 2010.

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